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PROTOCOL CONCERNING THE INTERPRETATION OF PARAGRAPH 7 OF THE PROTOCOL TO THE 1984 TAX AGREEMENT WITH THE PEOPLE'S REPUBLIC OF CHINA

MESSAGE

FROM

THE PRESIDENT OF THE UNITED STATES

TRANSMITTING

THE PROTOCOL, SIGNED AT BEIJING ON MAY 10, 1986, CONCERNING THE INTERPRETATION OF PARAGRAPH 7 OF THE PROTOCOL TO THE AGREEMENT BETWEEN THE GOVERNMENT OF THE UNITED STATES OF AMERICA AND THE GOVERNMENT OF THE PEOPLE'S REPUBLIC OF CHINA FOR THE AVOIDANCE OF DOUBLE TAXATION AND THE PREVENTION OF TAX EVASION WITH RESPECT TO TAXES ON INCOME, SIGNED AT BEIJING ON APRIL 30, 1984

JUNE 6, 1986.—Protocol was read the first time, and together with the accompanying papers, referred to the Committee on Foreign Relations and ordered to be printed for the use of the Senate

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LETTER OF TRANSMITTAL

THE WHITE HOUSE, *June 5, 1986.*

To the Senate of the United States:

I transmit herewith, for Senate advice and consent to ratification, the May 10, 1986, Protocol Concerning the Interpretation of Paragraph 7 of the 1984 Protocol to the Agreement Between the Government of the United States of America and the Government of the People's Republic of China for the Avoidance of Double Taxation and the Prevention of Tax Evasion with Respect to Taxes on Income, signed at Beijing on April 30, 1984. I also transmit the report of the Department of State on the new Protocol.

Senate consideration of the Agreement, which was transmitted for advice and consent to ratification by letter dated August 10, 1984, has been delayed in light of the concern expressed that it lacked strong "anti-treaty shopping" provisions. The 1986 Protocol remedies the situation by providing rules designed to prevent residents of third countries from investing through China in order to get the benefits of the income tax treaty.

It is most desirable that this Protocol, together with the Agreement, the 1984 Protocol thereto, and the related exchange of notes, be considered by the Senate as soon as possible and that the Senate give advice and consent to ratification of these instruments.

RONALD REAGAN.

LETTER OF SUBMITTAL

DEPARTMENT OF STATE,
Washington, May 20, 1986.

The PRESIDENT,
The White House.

THE PRESIDENT: I have the honor to submit to you, with a view to its transmission to the Senate for advice and consent to ratification, the Protocol Concerning the Interpretation of Paragraph 7 of the Protocol to the Agreement between the Government of the United States of America and the Government of the People's Republic of China for the Avoidance of Double Taxation and the Prevention of Tax Evasion with Respect to Taxes on Income, signed at Beijing on April 30, 1984. The new Protocol was signed at Beijing on May 10, 1986.

You signed the Agreement, with its related protocol and exchange of notes, at Beijing on April 30, 1984, and sent them to the Senate for advice and consent to ratification on August 10, 1984. While the Agreement was favorably reported out of the Senate Foreign Relations Committee in late 1985, some Senators expressed concern that it lacked adequate "anti-treaty shopping" provisions and, as a consequence, the agreement has not been brought to a full Senate vote. The new Protocol directly addresses these concerns by including rules which would prevent the use of the income tax treaty as a conduit by third country residents to obtain unintended treaty benefits. As a further related document, it should be given Senate advice and consent at the same time as the Senate advises and consents to the Agreement and related documents that you signed at Beijing.

A technical memorandum explaining in detail the provisions of the Protocol is being prepared by the Department of the Treasury and will be submitted to the Senate Committee on Foreign Relations.

Respectfully submitted,

GEORGE P. SHULTZ.

PROTOCOL CONCERNING THE INTERPRETATION OF PARAGRAPH 7 OF THE PROTOCOL TO THE AGREEMENT BETWEEN THE GOVERNMENT OF THE UNITED STATES OF AMERICA AND THE GOVERNMENT OF THE PEOPLE'S REPUBLIC OF CHINA FOR THE AVOIDANCE OF DOUBLE TAXATION AND THE PREVENTION OF TAX EVASION WITH RESPECT TO TAXES ON INCOME, SIGNED AT BEIJING ON APRIL 30, 1984

The Government of the United States of America and the Government of the People's Republic of China, desiring to conclude a Protocol in addition to the Agreement between them for the avoidance of double taxation and the prevention of tax evasion, and the supplementary Protocol attached thereto, have agreed as follows:

Both sides have agreed, with respect to the interpretation of Paragraph 7 of the Protocol to the Agreement, that their understanding is as follows:

1. A person (other than an individual) which is a resident of a Contracting State shall not be entitled under this Agreement to relief from taxation in the other Contracting State unless:

(a)(i) more than 50 percent of the beneficial interest in such person (or in the case of a company more than 50 percent of the number of shares of each class of the company's shares) is owned, directly or indirectly, by any combination of one or more of:

(A) individuals who are residents of one of the Contracting States;

(B) citizens of the United States;

(C) companies as described in subparagraph 1(b) of this protocol; and

(D) one of the Contracting States, its political subdivisions or local authorities; and

(ii) in the case of relief from taxation under Articles 9 (dividends), 10 (interest), and 11 (royalties), not more than 50 percent of the gross income of such person is used to make payments of interest to persons who are other than persons described in clauses (A) through (D) of subparagraph (a)(i), whether directly or indirectly; or

(b) it is a company which is a resident of a Contracting State and in whose principal class of shares there is substantial and regular trading on a recognized stock exchange.

2. Paragraph 1 shall not apply if the establishment, acquisition and maintenance of such person and the conduct of its operations did not have as a principal purpose the purpose of obtaining benefits under the Agreement.

3. For the purposes of paragraph 1(b), the term 'a recognized stock exchange' means:

(a) the NASDAQ System owned by the National Association of Securities Dealers, Inc. and any stock exchange registered with the Securities and Exchange Commission as a national se-

curities exchange for the purposes of the Securities Exchange Act of 1934; and

(b) any national securities exchange approved to be established by the Government of the People's Republic of China or its authorized institution; and

(c) any other stock exchange agreed upon by the competent authorities of the Contracting States.

4. Before a resident of a Contracting State is denied relief from taxation in the other Contracting State by reason of paragraph 1, 2 and/or 3, the competent authorities of the Contracting States shall consult each other.

This Protocol is certified for addition to the Agreement and its supplemental Protocol by the undersigned.

Done at Beijing on the 10th day of May, 1986, in duplicate, in the English and Chinese language, the two texts having equal authenticity.

JAMES A. BAKER III,
Secretary of the Treasury,
United States of America.

WANG BINGQIAN,
State Councillor and Minister of Finance,
People's Republic of China.

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